No. 95-608

(4)

Supreme Court, U.S.
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In The

Supreme Court of the United States

October Term, 1995

IN RE: HOLYWELL CORPORATION, MIAMI CENTER LIMITED PARTNERSHIP, MIAMI CENTER CORPORATION, HOLYWELL CORPORATION, CHOPIN ASSOCIATES, and THEODORE B. GOULD,

Petitioners,

v.

FRED STANTON SMITH, individually and as Trustee of the MIAMI CENTER LIQUIDATING TRUST; THE BANK OF NEW YORK; THE CITY NATIONAL BANK OF MIAMI, as Trustee under Land Trust #5008793; M.C. HOLDINGS PARTNERS, a New York General Partnership, and its General Partners, namely, ROBANK CORPORATION, H.D. LIQUIDATION, INC., ZENTAC INVESTMENTS, INC., BOTT FLORIDA HOLDING CORPORATION, AMERICAN SECURITY, LTD., and M. CENTER CORPORATION,

Respondents.

On Petition For Writ Of Certiorari To The United States Court Of Appeals For The Eleventh Circuit

REPLY BRIEF FOR THE PETITIONERS

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REPLY BRIEF FOR THE PETITIONERS

Introduction

The arguments presented in the briefs of the respondents mirror very closely those which they presented to this Court in the previous litigation. All of those arguments were rejected by the unanimous opinion of this Court. *Holywell Corporation v. Smith*, 503 U.S. 47, 112 S.Ct. 1021 (1992).

The briefs of the respondents present an inaccurate picture of the prior proceedings. In that instance, both the Solicitor General and your petitioner filed petitions which were merged for hearing. Contrary to the statements in respondents' briefs, the Court rejected the position of the Solicitor General, who had argued that this involved a bankruptcy trust, 112 S.Ct. at 1026.

Instead, the unanimous opinion of this Court was that Smith was the assignee[1] of substantially all of the property of Holywell Corporation. As such, his status was separate and distinct from his position as Trustee of

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[1] The Solicitor General conceded the historical significance of this Court's conclusion that the trustee was an "assignee" of the property of the corporate debtors. S.Ct. Transcript, December 4, 1991, p. 15. See *Thelusson, et al. v. Smith*, 2 Wheat 396, 425 (1817) [assignees are made personally responsible to the United States if, in the case of insolvency, they pay any debt previous to those due the United States]; *accord, Conard v. The Atlantic Insurance Company*, 1 Pet. 386, 439 (1828) [The United States has a right of prior payment from the debtor's funds in the hands of an assignee.]; *also Beaston v. Farmer's Bank of Delaware*, 37 U.S. (12 Pet.) 102, 136 (1838) ["the moment the transfer of property takes place, under the statute, the person taking it, whether by voluntary assignment or by operation of law, becomes bound to the United States for the faithful performance of the trust."]

the Miami Center Liquidating Trust. This Court distinguished this trust from trusts under the Bankruptcy Code and determined it was therefore not controlled by statutory provisions dealing with bankruptcy estates.

Respondents and the lower courts have chosen to ignore not only the parts of the decision of this Court which held that this was not a bankruptcy trust. They also ignore the opinion of the Eleventh Circuit, holding that the plan was not eligible to be confirmed, since it did not comply with the statutory requirements. *In re Holywell Corp.* (Bank of New York v. Olympia & York Florida Equity Corp., Theodore B. Gould, and Miami Center Joint Venture), 913 F.2d 873, 880 (11th Cir. 1990).

Similarly, the respondents have contended in the present proceedings that the trustee was relieved of his fiduciary duty, acting as an assignee of Holywell's property, to establish a reserve for the payment of income taxes prior to the commencement of distribution under the provisions of the Bank's plan "because the plan failed to disclose or provide for those taxes," Smith Br. 8, 10.

Respondents do not dispute that cash and securities of Holywell Corporation, and its nondebtor subsidiaries who were not before the court, were transferred to the trustee, in the amount of $27,806,529.18, as of October 11, 1985, under the provisions of the Bank's plan, or that the plan's substantive consolidation provision required the payment of Holywell's liabilities prior to its making a dividend distribution to the Miami Center Liquidating Trust to provide funds for the trustee's payment of claims against the other bankruptcy estates.

Respondents also do not dispute that the bankruptcy court's cash collateral order, entered on December 31, 1984, required the determination and payment of federal

income taxes from the funds transferred to the Trustee. C.P. 303; see also *Smith v. Bank of New York*, 161 B.R. 302, 304 (Bkrtcy. S.D. Fla. 1993).

Likewise, respondents do not dispute that the trustee commingled the accounting of the separate taxable entities in his fiduciary custody; failed to cause the repayment of the super-priority loans previously authorized by the bankruptcy court for the purpose of preserving and disposing of the Miami Center as the Bank's collateral, see 11 U.S.C. § 506(c); also Pet. 5, n. 7; compare *Smith*, 7; and failed to establish a reserve to cure the defaults under certain leases which had a priority superior to the Bank's liens, see 11 U.S.C. § 1123(d); also Pet. 6, 18, n. 19.

Similarly, the trustee does not deny that he sought personal indemnification from the Bank before proceeding, instead of following the established practice of asking the court's guidance in a formal hearing with respect to difficult questions with which he was faced in the administration of the plan.

Having received this indemnification, he then proceeded, in total disregard of the law, (a) to allow the Bank to take a credit against the Miami Center's purchase price, without an accounting, in an amount of at least $13,130,082.27 in excess of the debt payable under the notes, in violation of 11 U.S.C. § 502(b)(1), (b) to pay interest of $27,050,115.02 on the Bank's undersecured claim, and (c) to pay interest to other unsecured creditors, contrary to the provisions of the plan.

The Bank's plan required the Trustee to preserve and protect the property in his fiduciary custody and to manage that property in "all other ways as would be lawful for any person owning the same to deal therewith." However, respondents rely on a settlement negotiated

between the Bank and the Trustee to avoid scrutiny by this Court of their conduct and of the Trustee's use of the funds of the trust to pay taxes owed by a different entity (the corporate debtors), in order to avoid the Trustee's personal liability under 31 U.S.C. § 3713.

The respondents and the courts below have relied on the doctrine of estoppel in the remanded proceedings to be held in conformity with this Court's *Holywell* opinion, Pet. 16, n. 18, notwithstanding that this Court reversed the divided opinion of the Eleventh Circuit holding that the Trustee did not breach his fiduciary duty "under the terms of the [Bank's] plan or other statutory provisions." *In re Holywell Corp.*, 911 F.2d 1539, 1546 (11th Cir. 1990).

ARGUMENT

1. "The Judicial Apparatus . . . is a Great Respecter of Things that are Done . . . No Matter How Screwed Up"[2] – The postconfirmation proceedings have been characterized by pervasive personal bias,[3] complete disregard of the holding in this Court's opinion in *Northern Pipeline Construction Co. v. Marathon Pipe Line Co.*, 102 S.Ct. 2858 (1982),[4] and the amendments to the Bankruptcy Code

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[2] (Bkrtcy. S.D. Fla.) Chief Bankruptcy Judge Thomas C. Britton, Transcript, *Ex Parte* Conference, May 15, 1987, p. 48.

[3] Bankruptcy Judge Britton was required to recuse himself on August 27, 1987.

[4] The original complaint was removed from the State court and referred to a bankruptcy judge based on a pattern of conduct, as Bankruptcy Judge Britton explained it: "Take the entire jurisdiction of this [Bankruptcy] Court. The United States Supreme Court came out with a decision saying that only an

concerning the authority of a bankruptcy judge to hear causes of action cognizable only under state common law. See also 102 S.Ct. at 2881 (concurring opinion).

The respondents and the courts below have misunderstood the difference between a cause of action and the facts which show the violation of a right[5] to conclude that the original complaint represented core matters under 28 U.S.C. § 157, *In re Holywell Corp.*, 93 B.R. 780, 785 (S.D. Fla. 1988), affirmed, 881 F.2d 1086 (11th Cir.), *cert. denied*, 493 U.S. 1057 (1990).

Although 28 U.S.C. § 1452 provides for the removal of any cause of action to the district court if that court has authority to exercise jurisdiction over that cause of action under 28 U.S.C. § 1334, Pet. App. 44a,[6] there is no statutory authority or precedent for a district court to refer postconfirmation causes of action cognizable only at State common law to a bankruptcy judge. See 102 S.Ct. at 2870, n. 23, quoting *Murray's Lessee v. Hoboken Land & Improvement Co.*, 18 How. 272, 274 (1855); also *Granfinanciera, S.A. v. Nordberg*, 109 S.Ct. 2782, 2794 (1959), quoting *Schoenthal v. Irving Trust Co.*, 287 U.S. 92, 94-95 (1932) [Common law actions requesting money damages as relief "constitute no part of a proceeding in bankruptcy but concern controversies arising out of it."]

Article III judge can do what these judges do [but] . . . if it goes back to the Supreme Court . . . the Supreme Court's going to say it is okay . . . because it works." Transcript, May 15, 1987, p. 48.

[5] See *Baltimore S.S. Co. v. Phillips*, 274 U.S. 316 (1926).

[6] See 102 S.Ct. at 2872, n. 26, citing *Williams v. Austrian*, 67 S.Ct. 1443 (1947) [This cause of action could be adjudicated in federal court on the basis of its relationship to the reorganization proceeding.]

2. "This Court's *Holywell* Opinion Does Not Mean What It Says" – The contention of the respondents and of the lower courts that the provision of Federal Rule 60(b)(5) dealing with prior judgments is not applicable in this case defies the plain language of the rule. Here the Eleventh Circuit had affirmed the judgment of the lower court that the Trustee had no fiduciary duty to pay taxes, and this decision continues to be relied on, although the Eleventh Circuit's decision was reversed by this Court.

The district court had affirmed the decision of the bankruptcy court and held, under the doctrines of *res judicata* and collateral estoppel, that the petitioners were barred from relitigating the issue of the trustee's "failure to establish a reserve for the payment of income taxes [because] [t]he Bankruptcy Court held that the Trustee was not responsible for the filing of federal income tax returns on behalf of the Debtors or liable to the United States for the payment of any federal income taxes," 93 B.R. at 784.

Respondents now contend that "[t]he Supreme Court's tax decision has not changed the result of the debtors' prior unsuccessful attacks on the Trustee," Smith Br. 10, because this Court found that "[t]he plan said nothing about whether the trustee had to file income tax returns or pay any income tax due," 112 S.Ct. at 1024. There is, however, no provision in the Bankruptcy Code which specifically requires disclosure or any provision for the payment of postconfirmation tax liabilities. A plan must be proposed in good faith, 11 U.S.C. § 1129(a)(3), the plan must satisfy the Feasibility Standard, § 1129(a)(11), see Pet. 25, and the court may not confirm a

plan if the plan's principal purpose is to avoid the payment of taxes, § 1129(d).[7]

As we have previously explained, *supra* at 1, n. 1, the transfer of the property of the corporate debtors to the trustee as an assignee, 112 S.Ct. at 1025, imposed a fiduciary duty on Smith to establish a reserve and pay the taxes attributable to the income from the sale of Holywell's property prior to the use of such funds to pay claims against MCLP's estate. The trustee's breach of fiduciary duty was settled in this Court and could not be reexamined in the remanded proceedings required to be held in conformity with its *Holywell* opinion. *Supervisors v. Kennicott*, 94 U.S. 498 (1877).

3. "The Confirmation Order Has *Only* Been Reversed With Respect To The Plan's Treatment Of A Particular Claim." – The respondents' contention that the opinion on the merits of the court of appeals which affirmed the reversal by the district court of the bankruptcy court's order confirming the Bank's amended plan, see Pet. 9, could be construed as limited to the plan's treatment of a particular claim, Smith Br. 4, n. 6, defies the opinion's plain language, the mandate, and the provisions of the Bankruptcy Code.

11 U.S.C. § 1129 grants power to a court to confirm a plan "only if all" of the enumerated requirements in subsection (a) are met, and if "the plan does not discriminate unfairly, and is fair and equitable, with respect to *each class of claims or interest* that is impaired under and has not accepted the plan," § 1129(b) (Emphasis added).

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[7] The IRS concluded that the substantive consolidation provision of the Bank's plan was a scheme to evade the payment of taxes.

Section 1127(a) provides that a plan's proponent may modify a plan any time before confirmation "but may not modify such plan so that such plan fails to meet the requirements of section[s] 1122. . . . "

The Eleventh Circuit held that the Bank's amended plan discriminated unfairly with respect to the impaired claim of the Miami Center Joint Venture in violation of 11 U.S.C. § 1129(b)(1) and failed to comply with the requirements of 11 U.S.C. § 1129(a)(1), namely section 1122. 913 F.2d at 880.

Respondents do not dispute that the Bank has been unjustly enriched under the substantive consolidation provision of the Bank's amended plan and that the *Miami Center* mootness rulings[8] have been relied on to protect the trustee from personal liability. Instead, the trustee and the Bank contend that, under the Eleventh Circuit's *Miami Center* mootness doctrine, "it is too late to do anything about it," Smith Br. 11, Bank Br. 2.

In fact, no other court of appeals has adopted the *Miami Center* mootness rulings' reliance on the doctrine of finality. In *Matter of King Resources Co.*, 651 F.2d 1326, 1332 (10th Cir. 1980), quoting *Matter of Combined Metals Reduction Co.*, 557 F.2d 179, 186-91 (9th Cir. 1977), the Tenth Circuit addressed itself to matters which involved more than consummated sales and held that "[i]f we were to conclude that . . . the plan was erroneously confirmed by the district judge, then a decision to that effect could have some effect on the proceedings below. While much of the

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[8] *Miami Center Limited Partnership v. Bank of New York*, 820 F.2d 376 (11th Cir. 1987) (Miami Center I); *Miami Center Limited Partnership v. Bank of New York*, 838 F.2d 1547 (11th Cir. 1988) (Miami Center II), *cert. denied*, 488 U.S. 823 (1988).

debtor's property has been liquidated, and many of the creditors have been paid, the plan still controls the actions of the trustee. . . . As a result, we are of the opinion that the order of confirmation is not moot. . . . "

"[T]he federal courts have a 'virtually unflagging obligation . . . to exercise the jurisdiction given them.' " *Moses H. Cone Mem. Hosp. v. Mercury Constr. Corp.*, 460 U.S. 1, 15 (1983) (quoting *Colorado River Water Conservation Dist. v. United States*, 424 U.S. 800, 817 (1976)); see *England v. Louisiana State Bd. of Medical Examiners*, 375 U.S. 411, 415 (1964); *McClellan v. Carland*, 217 U.S. 268, 282 (1910); *Cohens v. Virginia*, 19 U.S. 264, 404 (1821).

"Only the clearest of justifications" warrant a federal court's decision to decline to exercise the jurisdiction provided by Congress, 424 U.S. at 819. Such justification includes, for example, a clear expression of congressional intent that jurisdiction should not be exercised. The doctrine of finality does not justify the abandonment of a court's duty to review an appeal's merits, see *McCarthy v. Madigan*, 112 S.Ct. 1081, 1087 (1992).

Civil liberty imposes an absolute duty on every court to decide cases and controversies on their merits. The constitutional requirement that a "real and substantial" case or controversy exists, see *North Carolina v. Rice*, 404 U.S. 244, 246 (1971), citing *Aetna Life Ins. Co. v. Haworth*, 300 U.S. 227, 240 (1937), does not provide the basis for avoiding the merits of difficult cases based on administrative convenience, and, as the Third Circuit Court of Appeals has held, "only two provisions of the Bankruptcy Code specifically require that a party seek a stay pending appeal," *In re Joshua Slocum, Ltd.*, 922 F.2d 1081, 1084 (3rd

Cir. 1990), and it is conceded that neither of these provisions was applicable to the trustee's conduct under the provisions of the Bank's plan, Pet. 7.

In the final analysis, respondents have no answer to the question of whether Rule 60(b)(5) requires the conclusion that it is no longer equitable for the *Miami Center* rulings to have prospective application to protect the trustee and unjustly enrich the Bank as the plan's proponent. It was clearly not equitable for the bankruptcy court in reliance on the Miami Center mootness ruling to have authorized the issuance of a Trustee's Certificate to the Bank, Pet. 18, n.19. The Bank's plan wrongfully subordinated MCJV's claim, 913 F.2d at 880, and the trustee failed to pay the claim in accordance with its superior priority, Pet. 15, also 23. Nevertheless, the Bank has imposed a postconfirmation liability in excess of $27,000,000 on the Trust estate and the trustee consented to the entry of the judgment against him.

For the foregoing reasons, and for the reasons stated in our petition, the petition for a writ of certiorari should be granted.

Respectfully submitted,

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